

**BEFORE THE PUBLIC UTILITIES COMMISSION
OF THE STATE OF CALIFORNIA**

Order Instituting Rulemaking to Oversee
the Resource Adequacy Program, Consider
Program Refinements, and Establish
Annual Local Procurement Obligations

Rulemaking 11-10-023
(Filed October 20, 2011)

**COMMENTS OF THE
ALLIANCE FOR RETAIL ENERGY MARKETS
ON PROPOSED DECISION**

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The Alliance for Retail Energy Markets (“AReM”) ¹ submits these comments on the proposed *Decision Adopting Local Procurement and Flexible Capacity Obligations for 2015, and Further Refining the Resource Adequacy Program* (“PD”) issued on May 27, 2014 in this rulemaking by Administrative Law Judge David M. Gamson of the California Public Utilities Commission (“Commission” or “CPUC”). These comments are timely filed and served pursuant to Rule 14.3 of the Commission’s Rules of Practice and Procedure.

I. INTRODUCTION

AReM has been an active participant in this proceeding leading up to the PD, and supports many of the Resource Adequacy (“RA”) program modifications that are included in it (as discussed in Section III of these comments). However, AReM continues to believe that there are compelling reasons, discussed fully in Section II of these comments, why the Commission should defer enforcement of the flexible capacity requirement for the 2015 RA year. When these

¹ AReM is a California non-profit mutual benefit corporation formed by electric service providers that are active in the California’s direct access market. This filing represents the position of AReM, but not necessarily that of a particular member or any affiliates of its members with respect to the issues addressed herein.

facts are considered, along with the fact that there is an undisputed abundance of flexible capacity available to the CAISO (and therefore little risk to system reliability in the absence of flexible capacity procurement enforcement in 2015), AReM believes that the Commission must make the decision that the potential costs, including the costs of non-compliance, that will result from enforcement of the flexible capacity requirements are simply not warranted. Therefore, AReM respectfully requests that the PD be modified accordingly to defer compliance with the flexible capacity requirements until the 2016 RA compliance year. The requested modifications to the PD are shown in Attachment A.

II. ENFORCING FLEXIBLE CAPACITY REQUIREMENTS FOR 2015 WILL LEAD TO INEFFICIENT PROCUREMENT.

AReM recognizes that the Commission is fully committed to modifying California's RA procurement obligations to include flexible capacity in order to better integrate the increasing amount of intermittent renewable energy that are interconnected to the electric grid. This RA program design is, without a doubt, going to increase customers' costs, and as such, should be implemented in a way that leads to effective and efficient procurement by all Load-Serving Entities ("LSEs"). The development of flexible capacity requirements and the integration of those requirements into the RA program have required (and will continue to require) unprecedented levels of cooperation between the staffs of the CPUC and the California Independent System Operator ("CAISO"), as both organizations retain jurisdiction over different elements of enforcement of such requirements. Despite the valiant and ongoing efforts to set forth clear details to govern the implementation of flexible capacity requirements, AReM is convinced that the policies and systems necessary for efficient implementation of these new

requirements are not yet at a stage of readiness that allows for effective or efficient procurement of flexible capacity for the 2015 RA year – *i.e.*, not ready for “prime time.”

The rationale for a deferral of enforcement of the flexible capacity compliance obligation is as follows.

A. The CAISO Is Not Prepared to Enforce the Must-Offer Obligation.

The CAISO continues to vet tariff language with respect to the must-offer obligation that flexible RA capacity resources must meet and, therefore, tariff language to codify these requirements has yet to be submitted to the Federal Energy Regulatory Commission (“FERC”). Based on the schedule established by the CAISO for finalizing the tariff language, AReM believes that submission of tariff language to FERC is about one month away, sometime in July.² While AReM can appreciate the thoroughness with which the CAISO is developing its must-offer requirement, the fact is that, without a must-offer obligation in place, flexible capacity purchased by LSEs – and paid for by their customers – will have no corresponding performance obligation. The LSEs and their customers will be paying for nothing.

In order to meet compliance deadlines, contracting for flexible capacity for the 2015 RA year must get done by October of 2014; obviously, the CAISO’s tariff filing will remain pending at FERC for much if not all the summer and early fall of 2014. It will not be known whether any parties are protesting any aspect of the CAISO’s tariff filing for about 20 days after the tariff filing is made – sometime in late July or early August. While it conceivable that the CAISO’s tariff could be in place by the start of the 2015 RA year, it is not going to be in place at the time contracting for flexible capacity gets underway with the adoption of this PD by the Commission.

² The CAISO said at its June 12, 2014 stakeholder meeting on the Reliability Services Initiative that it will be submitting revised tariff language for market participant review during the week of June 16, and will conduct another stakeholder call to review the changes in the week or so following that.

Lack of certainty about the enforceability of the must-offer obligation will compromise and complicate RA contracting, increasing the potential for unintentional non-compliance.

The Commission should not allow a situation to unfold where its jurisdictional LSEs purchase capacity that in turn has no performance obligation. Given the uncertainty about whether the CAISO will have an enforceable must-offer obligation in place for the 2015 year, it is clear to AReM that the best way to avoid that outcome is to defer procurement compliance obligation for flexible capacity to the 2016 RA compliance year.

B. The Information Necessary for LSEs to Manage their Procurement of Effective Flexible Capacity Will Not Be Available, Creating Unacceptable, Unnecessary, and Potentially Costly Compliance Risks.

The CAISO publishes the Net Qualifying Capacity (“NQC”) list each year. This list informs buyers and sellers of capacity of system and local RA quantities that each unit on the list is capable of providing. As such, it facilitates RA transactions by providing market participants with information about what resources are qualified to meet the RA obligations and how much RA each resource can provide. The new flexible capacity requirements create a new category of RA, referred to as the Effective Flexible Capacity (“EFC”), essentially a third category in addition to system and local RA. The CAISO has stated that it will publish a list of resources that can provide EFC each year, with a draft list available by September 1, and a final list available on October 1 of each year.³ There are two problems associated with the EFC list.

First, AReM has previously requested that the CAISO publish the EFC list to match the publication of the NQC list with the preliminary list available on May 1, and the final list available on September 1. However, the CAISO has not agreed to make this change. Having final EFC information available on October 1, when final RA filings are due October 31, is

³ See, CAISO Draft Tariff Language, Section 40.10.4, issued May 19, 2014.

wholly inadequate, particularly in the first year of compliance when there are many contracting issues to address. AReM believes that, for at least the first two years of enforceable flexible capacity requirements, the final EFC list should be available no later than June 1 of the prior year. Obviously, that criterion cannot be met for the 2015 RA compliance year.

Second, the EFC list is not being structured to provide market participants with the information they need to manage their RA contracting. Specifically, the flexible capacity obligation that will be assigned to LSEs includes a requirement that at least 68% of the EFC requirement be met with base flexibility resources (Category 1) from May through September, and 74% for January – April and October – December.⁴ The remainder of the EFC obligation can be met with resources that fall into one of two lower levels of flexibility, referred to as Category 2 and Category 3. The extent to which a resource that is eligible to provide EFC meets each of the three categories of flexibility is not available to market participants, and the CAISO has said that it has no intention of including this information on the EFC list. The CAISO insists that contractual RA counterparties can figure that out for themselves, and include appropriate indemnifications and assignment of compliance risks in their RA contracts. The CAISO has stated, however, that it plans to verify whether LSEs have purchased the appropriate quantities of each category when it performs its validation process after compliance showings are made. In short, LSEs are being required to purchase EFC in particular categories, are not being given information that allows them to determine whether a particular counterparty is able to provide EFC in any particular category, but will be held accountable for failing to procure the right amount in the right category based on the CAISO's assessment of whether the specific resources

⁴ PD, pp. 12-13, p. 19, p. 20, and Ordering Paragraph 4, p. 72.

referenced in the compliance showing can actually meet the Category specifications for which it has been purchased.

AReM does not understand the CAISO's reticence to provide this information. Without it, there is the risk that LSEs will procure RA in an amount that they believe to achieve full compliance, only to find out that it does not, and then be subject to potentially costly CAISO backstop procurement. Such an outcome should not be allowed. If the CAISO intends to validate compliance showings against this requirement, and has the information to do so, it should make that information available on the EFC list. Unless and until the CAISO makes this information available, LSEs should be insulated from any potential compliance penalties associated with failure to procure flexible capacity in the right categories. The problem here resides with the CAISO, but the Commission should not turn a blind eye to the importance of this issue and the impact that the CAISO's position in this matter will have on RA contracting and compliance. Put simply, the Commission should consider the CAISO's intractable position as one important reason why flexible capacity procurement compliance enforcement should be deferred until 2016. If the Commission does not defer enforcement of the flexible capacity requirements for the 2015 RA year, AReM requests that the PD be modified to expressly state that it will impose no penalties or backstop procurement costs on an LSE whose compliance showing misses the mark for the EFC categories.

C. The Commission's Stated Plan to Consider Significant Modifications to the Flexible Capacity Program Over the Next Year Will Limit the Effectiveness of Near-Term Procurement.

Section XI of the *Adopted Flexible Capacity Procurement Framework*, set forth in Appendix A of the PD specifies the following next steps for 2016 RA Year:

1. Explore a flexible capacity allocation methodology that reflects causation.

2. Comprehensively reform the RA procurement framework and adopt rules that simplify the compliance process.
3. Further assess if the three flexible categories address the objective of managing use-□limited resources and allowing the participation of preferred resources and the appropriateness of characteristics for each category.
4. Explore the possibility of exempting flexible resources from satisfying system RA requirements, but will assess the overall impact on contracting, procurement, and must-□offebligations before recommending this policy.⁵

Taken together, these next steps indicate that every single aspect of the flexible capacity RA program will be under review in 2015 and that significant changes are likely. With this comprehensive list of next steps on the drawing board, any procurement that does get done for 2015 RA year compliance will, of necessity, be for no more than the 2015 compliance year. Therefore, enforcement of the compliance obligation in 2015 will do little in terms of incenting any flexible capacity procurement for the longer term, when the CAISO's forecast show there to be a genuine need for flexible capacity. The upshot is that there will be very little benefit in 2015 at potentially high costs. Any of these revisions, if adopted, could create a fundamental change in the procurement of RA and should be resolved before procurement obligations are enforced.

Looking individually at the next steps, AReM notes that item 1, which involves exploring a flexible capacity allocation methodology that reflects causation, could have a fundamental impact on contracting for flexible capacity. Specifically, AReM understands that the discussions on this topic may consider whether some (or all) of the flexible capacity requirement will be directly imposed on flexible resources as a way to better reflect cost causation. AReM does not

⁵ See pp. A-12 to A-13 of Attachment A to the PD.

have a position on this issue at this time. However, AReM believes that changes in the overall allocation methodologies should be resolved before procurement obligations are enforced.

Similarly, item 4, which will explore a possible exemption from meeting system RA requirements for flexible resources, could create a fundamental change in the procurement of RA and should be resolved before flexible capacity procurement obligations are enforced for LSEs.

D. The CPUC and CAISO Have Yet To Reach Agreement On Important Details of the Flexible Capacity Requirement, Creating Unacceptable, Unnecessary, and Potentially Costly Compliance Risks.

AReM recognizes that there are a few remaining discrepancies between the CPUC's and CAISO's implementation of the flexible capacity requirements, particularly with respect to how energy storage and supply-side demand response resources will be counted and included.⁶ AReM has not been able to assess the full impact of the remaining discrepancies. Nevertheless, the fact that the discrepancies exist raise the possibility that a compliance showing could pass muster for the CPUC, while failing at the CAISO (or vice versa). This should not be allowed to occur, as it creates significant contracting complexities that should be avoided – *i.e.*, do contractual indemnifications apply to meeting the CPUC requirements or the CAISO requirements? If compliance is not deferred for the 2015 RA year, then the Commission should ensure that it will not enforce compliance penalties for an RA showing that is compliant with CAISO requirements, even though non-compliant with CPUC requirements, until the differences between the two programs are resolved.

⁶ See, discussion in the PD, pp. 15-16, p. 28.

III. THE APPLICABLE NON-COMPLIANCE PENALTY FOR FLEXIBLE CAPACITY SHOULD BE THE LOCAL RA PENALTY.

The PD adopts Energy Division’s proposal to apply system RA penalties for non-compliance of the flexible capacity procurement requirements.⁷ System RA penalties, at \$6.66/kW-month, are twice those for local RA (\$3.33/kW-month) and are applied when an LSE fails to procure to meet its requirements within the five-day cure period.⁸ Applying the larger system RA penalty to flexible capacity procurement is unreasonable, considering the uncertainties discussed above, such as the lack of timely and complete EFC information from the CAISO and the discrepancies between the CPUC and CAISO rules. Accordingly, AReM requests that the local RA penalty be applied to non-compliance with flexible capacity procurement requirements for the first year of compliance (whether 2015 or 2016) and be re-assessed at that time. Appendix A provides the suggested modifications to the PD to implement this change.

IV. AReM GENERALLY SUPPORTS OTHER DETERMINATIONS IN THE PROPOSED DECISION BUT SEEKS ONE CLARIFICATION.

In general, AReM finds the remainder of the PD reasonable and, in particular, supports the following determinations:

A. Scheduled Outage Replacement Rule and Standard Capacity Product Mechanisms for Cost Allocation Mechanism (“CAM”) Resources and Combined Heat and Power (“CHP”).

AReM supports the PD’s adoption of Energy Division’s revised proposal with the additional clarifications cited.⁹ In particular, AReM appreciates the PD’s recognition of the

⁷ See, Attachment A to the PD, p. A-9.

⁸ These penalties were established in D.10-06-036, Ordering Paragraph 6.g, p. 65.

⁹ PD, pp. 48-49.

potential for cost shifting in rejecting Southern California Edison’s proposal to recover costs for replacing “like” CAM or CHP resources shown in their RA filings.¹⁰

B. CAM and CHP Resources Procured Outside the Procuring Utilities’ Service Areas and the Path 26 Constraint.

AReM concurs with the PD’s adoption of the Revised Staff RA Refinement Proposal¹¹ and the rejection of San Diego Gas & Electric Company’s proposal to grandfather CHP contracts that are unable to be netted.¹² However, AReM finds the discussion in the PD unclear. Specifically, AReM seeks clarification of the following phrase:

“The additional available Path-26 capacity created by netting of these CHP contracts would be allocated to LSEs based on the LSEs netting participation-ratio share **and no longer based on LSEs’ load-ratio.**” (emphasis added)¹³

AReM assumes this modification and its implementation is not intended to disadvantage electric service providers (“ ESPs”) or their direct access customers will by implementation of this proposal. AReM requests that the PD be modified to make this clear, as set forth in Appendix A. In addition, AReM requests that Staff provide an example explaining the mechanics of the proposal during the workshop or meeting held to discuss implementation for the 2015 RA compliance year.

¹⁰ PD, p. 49.

¹¹ PD, p. 41.

¹² PD, p. 42.

¹³ PD, p. 40.

C. Allocation of Flexible Capacity for CAM and CHP Resources.

AReM strongly supports the PD's requirement that allocations be made by Flexible Capacity category.¹⁴ As the PD notes, failing to provide such information to the LSEs risks "misalignment" between the CPUC and CAISO programs.

D. Aggregation of Local RA Requirements.

The PD rejects Energy Division's proposal to allow LSEs to aggregate Local RA Requirements in an IOU's service area where an LSE has Local RA Requirements of less than 5 MW.¹⁵ AReM concurs. As AReM previously noted, meeting RA obligations is a fundamental compliance obligation that all LSEs should be prepared to meet.¹⁶ Further, the Commission has established several safeguards when creating its Local RA program, such as a waiver trigger price, aggregation of some of the local capacity areas in the service territory of Pacific Gas and Electric Company, and exemptions for LSEs with requirements less than 1 MW. These mechanisms should be sufficient and further exemptions from procurement based on the size of the LSE should not be implemented, as direct exemptions create issues of free ridership.

V. CONCLUSION

AReM appreciates the opportunity to present these comments and urges the Commission to adopt AReM's recommendations as follows:

- ∞ Defer compliance with flexible capacity requirements until the 2016 RA compliance year to provide time for the CPUC and CAISO to develop and

¹⁴ PD, p. 53.

¹⁵ PD, p. 57.

¹⁶ See, *Comments of the Alliance for Retail Energy Markets on Energy Division's Proposals*, R.11-10-023, February 18, 2014, pp. 7-8.

implement uniform rules and provide timely information critical for efficient procurement.

- ∞ Apply the lower local RA penalty for non-compliance with the flexible capacity procurement requirements for the first year of compliance (whether 2015 or 2016) in consideration of the uncertainties of the new program.
- ∞ Revise the PD to state that non-utility LSEs and their customers are not to be not be disadvantaged by implementation of the Path-26 netting proposal.

Respectfully submitted,



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ATTACHMENT A

RECOMMENDED MODIFICATIONS TO PROPOSED DECISION

Modification to Attachment A of PD, p. A-3

For the 2015 RA year, we will use load-ratio share to allocate flexibility among LSEs. **However, for 2015, the flexible capacity requirements will be targets only and will be mandatory starting with the 2016 RA compliance year.** In the future, we intend to explore other methods of allocation based on causation through the RA proceeding, potentially in conjunction with staff's analysis of reliability needs. An LSE's flexible procurement obligation is calculated as follows, consistent with how system and local RA requirements are allocated.

Modifications to Findings of Fact

New Finding of Fact 15: Energy Division staff should use the time between now and June 2015 to refine a flexible capacity framework for mandatory implementation in RA year 2016 and conduct the next steps identified in the Adopted Flexible Capacity Framework contained in Attachment A, providing time for the CAISO to finalize implementation of its flexible capacity tariff revisions.

New Finding of Fact 16: The Adopted Flexible Capacity Framework in Attachment A, should be interim for 2015 in order to determine the efficacy of the framework and consider additional flexibility requirements, and should be mandatory starting with RA compliance year 2016.

Modifications to Conclusions of Law

1. The CAISO's 2014 Local Capacity Technical Analysis Final Report and Study Results should be approved as the basis for establishing local procurement obligations for 2015 applicable to Commission jurisdictional LSEs **and should be mandatory starting with RA compliance year 2016.**

13. Energy Division should implement the RA program for ~~2015~~ **2016** in accordance with the adopted policies in this and previous decisions.
14. It is reasonable to ~~impose a~~ **defer imposing a mandatory** new requirement on LSEs for flexible capacity starting in the 2015 RA year.
15. It is reasonable to cause increased ratepayer costs by imposing a flexible capacity requirement starting in ~~2015~~ **2016** because there will be commensurate or greater benefits from improved reliability.

Modification to Ordering Paragraph

9. The Resource Adequacy program is modified so that additional available Path -26 capacity created by the netting of existing contracts shall be allocated to load-serving entities (LSEs) based on the LSE's netting participation-ratio share, and shall no longer be based on LSEs' load-ratio. **This modified approach is intended not to disadvantage any non-utility LSEs.**